United States Court of Appeals

for the Second Circuit

APPELLANT'S REPLY BRIEF

ORIGINAL

76-7281

United States Court of Appeals
For the Second Circuit

B

P/S

PRESCRIPTION PLAN SERVICE CORPORATION,
Plaintiff-Appellant,

-against-

ALBERT FRANCO, individually and as Administrator, SHANNON J. WALL, MARTIN F. HICKEY, MEL BARISIC, F.K. RILEY, Jr., RICK MILLER, E. MARCUS, JAMES J. MARTIN, W.I. RISTINE, PETER BOCKER, E.G. DENYS, ANDREW RICH and KENNETH W. GUNDLING, individually and as Trustees of the NMU PENSION & WELFARE PLAN,
Defendants-Appellees.

On Appeal From The United States District Court For The Southern District Of New York

APPELLANT'S REPLY BRIEF

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UNITED STATES COURT OF APPEALS
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Statement

In this reply brief we shall endeavor to rebut those assertions and arguments advanced by appellees' briefs (hereinafter "Franco Brief" or "Employer Brief" for the brief filed for appellees Franco and the employer appointed trustees; and "Wall Brief" or "Union Brief" for the brief for the appellee Wall and the other Union appointed trustees) which we feel have not been squarely met or anticipated by our main brief or the

Joint Appendix. We do not propose to burden this Court with a re-exposition of arguments already made, and, by the same token, our omission in this brief to answer every argument advanced by appellees' briefs is not to be taken as a concession of validity.

The Statements of the Case

Our position is that having filed the complaint on October 23, 1975 (10a), and having received the applications of all of the named defendants for jurisdictional dismissal in late December 1975 following two successive stipulations with counsel for all of the named defendants for extension of time, the appellant ("PPS") was entitled to defend against the jurisdictional onslaught by asserting its primary reliance on the federal nature of the first cause of action for fraud and deceit (with valid pendent jurisdiction over the second, related, contract cause of action), a secondary position arguing the dispensibility of the assertedly New York defendants under the criteria of Rule 19, FRCP, in the interest of saving the diversity jurisdiction of the district court over both causes of action (which is where the "federal flavor of the case" was urged - in a diversity context - as a consideration additional to those set forth by Rule 19, FRCP), and, a tertiary position for retention of the first cause of action against the non-resident defendants only insofar as they were being sued in tort as individuals.

With the jurisdictional setting fixed as it existed on the date of filing the complaint, it was obviously in the interest of orderly procedure for the appellant to wait on judicial determination, including this appeal, of where it stood

with reference to the jurisdictional issues of the case before undertaking fresh moves by way of service of process, instituting new actions, discontinuing old ones, etc., etc.

It therefore comes with poor grace for the Franco Brief to say in its long footnote at page 5:

> " * * * This admission by PPS that it failed to effect proper service on any of the defendants should, in itself, be dispositive of this appeal. Absent valid service of process, the District Court could not have acquired personal jurisdiction over the defendants. This alone required dismissal of the complaint for lack of personal jurisdiction. Similarly, since the District Court lacked personal jurisdiction over the defendants, there was no basis upon which it could have entertained PPS's cross-motion to amend the caption. Thus, PPS's cross-motion was properly denied. If PPS wished to change the caption and effect proper service of its complaint, then it should have discontinued the action and served a new complaint without burdening this Court with this appeal."

The above attempt at whipsaw tactics is repeated in the Union Brief at page 15:

> " * * * Plaintiff has conceded this lack of personal service (73a) and has not remedied this deficiency even after it has been called to its attention. Thus, consideration of the merits vel non of plaintiff's claim of individual responsibility is clearly premature.

All of this lends credence to our notion that, pried loose from the tableau of residence and official capacity as it existed on October 23, 1975, the going would not be easy for PPS to reestablish its causes in new quarters; for all of their outcry of indispensibility of all of the trustees, the appellees have stoutly denied the jurisdiction of any court - state or federal - to acquire long arm jurisdiction of former trustees Marcus and Denys. And, while keeping discreet silence as to the identity or "indispensibility" role of the two replacement trustees (Franco Brief, p. 3), when the time is ripe, that too can be reliably depended upon to be thrown in as a stumbling

block for PPS. Here the overkill only lends validity to and underlines the strong force for applying the fourth criterion of Rule 19(b), FRCP, and the special emphasis given to it in Provident Tradesmens Bank v. Patterson, 290 U.S. 102 (1968) by Mr. Justice Harlan's opinion as quoted at page 15 of our main brief.

Appellees' Statement of the Facts

The most serious distortion of the statement of facts in the Franco brief (pp. 6-11) is its attempt to capitalize on an oversight with respect to the application of the minimum guaranteed service fee provided for by one of the terms of the January 11, 1975 service agreement between PPS and the NMU Pension & Welfare Plan (45a-47a).

Thus the Franco brief at p. 10:

> "PPS's second cause of action is based upon an alleged breach by defendants of the January 11, 1975 agreement. PPS claims that it was entitled to receive one-sixth of the minimum service fee provided therein ($1.50 x 24,632 members = $36,948 for the six month period of the agreement) for any month after the termination of the agreement in which it continued to process prescriptions for Plan members. However, the plain language of the agreement provided that the minimum service fee guarantee was applicable only to the six month period during which the agreement was in effect. (Agreement ¶2, 46a)."

The limitation of the minimum service guarantee payment to the six month period from January 1, 1975 to June 30, 1975 is incorrect - and the plain language of the agreement shows that the two six month periods of calendar year 1974 were also explicitly covered by the guarantee of minimum payment. Thus at 46a:

> "1. The Agreement between the parties dated January 29, 1974 is hereby extended for a period of six months from January 1, 1975 to June 30, 1975 with the following changes.

"2. Paragrapn 6 of the Agreement dated January 29, 1974 is amended to add the following sentence:

> 'If during any six month period that this Agreement is in effect the amount payable to PPS for processing claims as set forth herein shall be less than the amount computed by multiplying the number of eligible members enrolled in the Plan at the commencement of such six month period by $1.50, then PPS shall be paid the amount so computed as its fee for processing all claims during said period.'"

and, in reference to paragraph 6 of the Agreement of January 29, 1974 (37a-44a) at 40a:

> "6. During the first and third week of each month after the effective date of the drug program, PPS shall submit to the Plan a statement of charges for prescriptions (computed as provided in paragraph 5 above) processed during each two week period, together with a copy of each prescription form constituting the basis upon which the statement of charges was computed. Upon receipt and acceptance of such charges, the Plan shall remit to PPS the total of such charges plus fifty cents ($.50) for each claim processed or rejected during such period. PPS warrants and agrees that it will pay the participating pharmacies the sums to which they are entitled not later than 20 days after receipt of such funds from the Plan."

and, in reference to the term covered by the Agreement of January 29, 1974, at 43a:

> "13. This Agreement shall remain in full force and effect for a period of one year from January 1, 1974 and will automatically be extended on the first anniversary date, provided however, that either party to this Agreement may terminate the Agreement at any time after the first anniversary date, such termination to be effective 60 days after the giving of written notice to either party. The termination of this Agreement shall not effect the continuing obligations of either party with respect to claims incurred for prescription drug benefits by eligible members during the term of this agreement.

The fact that the Franco brief argues the limitation of the minimum guarantee payment to the first six months of 1975 also confirms that the Plan has made no such payment for either six month period of 1974, and the complaint will accordingly be amended as of right under Rule 15(a), FRCP, to reflect

damages for that breach.

POINT I

IN SPITE OF THE FACT THAT THE FIRST CAUSE OF ACTION IS CLAIMED BY PPS AS A COMMON LAW TORT COGNIZABLE UNDER THE FEDERAL QUESTION JURISDICTION OF THE DISTRICT COURT, BECAUSE THE FRAUD AND DECEIT PRACTICED HERE CONSTITUTES AND IMPLEMENTS THE COMMISSION OF TAFT-HARTLEY MISDEMEANORS - EXCLUSIVELY FEDERAL - APPELLEES NEVERTHELESS PERSIST IN THE MAKE BELIEVE THAT PPS IS MISTAKENLY PURSUING STATUTORY CAUSES OF ACTION.

The Franco brief (pp. 13-31) is notable for the elaborate extent to which it goes to demonstrate that no statutory action is available here to PPS, a point which we readily concede. We have made it abundantly plain that the first cause of action pleaded in the complaint is a common law action for fraud and deceit that would be actionable, without reference to a substantive statute, in any forum that entertains it. Yet, every time the Franco brief acknowledges that fact, it hurries on to distort it by tagging the false label of "statutory" action upon it. Thus at p. 18:

> "In a desperate attempt to bring otherwise straightforward claims of fraudulent inducement to enter into contractual relations and breach of contract within the scope of Section 302 of the LMRA, PPS has made bald, unsupported allegations that defendants were involved in a 'scheme' to divert trust fund monies and apply such monies for improper purposes * * * . However, such an allegation is totally irrelevant because Section 302 has no applicability whatsoever to alleged violations of fiduciary duties or standards of prudence in the administration of trust funds, such claims being governed by state law. * * * "

Aside from the fact that we have never asserted that our second cause of action for breach of contract had any independent standing as a federal cause of action, much less a statutory one, both the Franco brief and the Union brief (p.7)

seem to urge that the only proper subjects of federal question jurisdiction are statutory actions by statutory beneficiaries pursuing statutory remedies. In doing so the appellees ignore the disjunctive standards set forth in the passage quoted at page 15 of the Franco brief from Lindy v. Lynn, 501 F. 2d 1367, 1369 (3rd Cir. 1974):

> "An action arises under the laws of the United States if and only if the complaint seeks a remedy expressly granted by a federal law or if it requires the construction of a federal statute or a distinctive policy of a federal statute requires the application of federal legal principles for its disposition. * * * Here the dispute between the parties is purely one as to the correct interpretation and effect of certain contractual documents, an ordinary contract dispute to be determined by the application of the principles of contract law." (emphasis supplied)

The large diversion of trust funds to Union aggrandisement which we allege is not "a simple breach of fiduciary duty to a § 302(c) trust" of Haley v. Palatnik, 509 F. 2d 1038, 1040 (2d Cir. 1975), nor the incidental non-compliance of the Taft-Hartley trustees with the requirements of LMRA's section 302, or of the Employees' Retirement Income Security Act of 1974 (ERISA), 29 U.S.C. § 1100, et seq., in the suit for an unrepaid overdraw which is Hibernia Bank v. Intl. Brotherhood of Teamsters, 411 F. Supp. 478 (N.D. Cal. 1976). At the risk of being monotonous, a massive diversion of trust assets from its legitimate applications and objects to a Union's purposes and applications, to our mind at least, represents the commission of the federal crimes defined in section 302 of Taft-Hartley which we think quite obviously represent "a distinctive policy of a federal statute /which7 requires the application of federal legal principles for its disposition." And where as here, a fraud and deceit are practiced which is an

implementing part and parcel of that criminal diversion, the result is a case so permeated with federal law which ought exclusively to be construed by the federal courts, as to constitute a federal question case.

With respect to federal common law, Weinberger v. New York Stock Exchange, 335 F. Supp. 139 (SDNY 1971) allowed a switch from a time-barred statutory action so that the plaintiff could bring his cause in the vestments of a third-party beneficiary to a contract and thus have the advantage of being timely under the more liberal contract statute of limitations. The principles enumerated in Weinberger have, if anything, been extended in Van Gemert v. Boeing Co., 520 F. 2d 1373 (2d Cir. 1975) where this Court, per Oakes, J., said at p. 1380:

> "The claim that Boeing is civilly liable under federal law for violation of the NYSE Listing Agreement * * * is a colorable one. * * * In O'Neill v. Maytag, 339 F. 2d 764, we did say, however, in the context of a stockholder's derivative suit arising out of an air carrier's purchase of its own stock, that a transaction which violated an Exchange rule did not give rise to a cause of action under federal law, at least against a listed company or its officers.
>
> "But as the Supreme Court held in J.I. Case Co. v. Borak, 377 U.S. 426 (1964), private parties have both derivative and direct rights of action to bring suit for violations of the Securities Exchange Act of 1934 and SEC rules and regulations issued thereunder, rights the explication of which take up a fair amount of Second Circuit judicial time. We extended this at least by dictum to include violation of stock exchange and security dealers' association rules designed for the direct protection of investors, at least in a suit against an Exchange member, in Colonial Realty Corp. v. Bache & Co., 358 F. 2d 178 (2d Cir.), cert. denied, 385 U.S. 817 (1966). * * * "

And, at p. 1381,

> "Nevertheless, we do not now take the position that appellees advance and the court below apparently accepted, that violation of an exchange rule cannot under any circumstances give rise to civil liability under the federal acts. Such a position would be in conflict withour own

most recent statements on this subject as well as some of the developing case law. * * * *

"It would also run contrary to a position we find inviting, that to the investing American public listing on the New York Stock Exchange carries with it implicit guarantees of trustworthiness. * * * "

Sophisticated transfers and diversions of Taft-Hartley trust funds from their statutorily legitimate trust purposes to the uses and purposes of the Union sponsor are wrongs, misdemeanors in fact, unknown to the common law. Against that backdrop of strong federal statutory policy, the first cause of action should proceed in the only court competent to try it.

POINT II

THE APPELLEES CANNOT REBUT THE ENDEAVOR OF PPS TO PRESERVE THE DIVERSITY JURISDICTION OF THE COURT BY ARGUING THE OBVIOUS, i.e., THAT IN THE ABSENCE OF COMPLETE DIVERSITY BETWEEN PARTIES, THERE IS NO DIVERSITY JURISDICTION AT ALL.

Once again the appellees (Franco brief, pp. 31-41; Union brief, pp.9-15) go to great lengths to demonstrate the off-point and uncontested obvious, i.e., that unless there is complete diversity of of citizenship between the adverse parties, there is no diversity jurisdiction of the cause in the federal courts, and whether the authority cited for the proposition is at the pinnacle, Blake v. McKim, 103 U.S. 336 (1881), or on the floor, Sanders v. Birthright, 172 F. Supp. 895 (S.D. Indiana 1959), it is only the starting point of reference from which the real issue on this point - the dispensibility or indispensibility of the allegedly resident trustees for joinder purposes - turns.

We have already shown that, by the explicit language

of Rule 19, FRCP, and of Harlan, J., in Provident Tradesmens Bank v. Patterson, 390 U.S. 102, 108, 109 (1968) the effect of an otherwise desirable joinder on the retention or ouster of the district court's jurisdiction of the case is a matter of the utmost importance, with ouster to be avoided if at all possible. Further, Rule 19, FRCP, sets forth eight intensely practical criteria for balancing the equities for and against joinder, not the least of which is the fourth criterion of Rule 19(b) as to the consequences to the cause of a jurisdictional turnout. Further still, it was demonstrated in Booth v. Security Mutual Life Ins. Co. 155 F. Supp. 755 (D. N.J. 1957), and in the New York state cases, that concepts of indispensibility are to be measured by the practicalities of a situation where the alternative stops or cripples the action.

That equitable considerations govern the requirement or waiver of joinder in particular cases is not new. Caylor v. Cooper, 165 Fed. 757 (SDNY 1908), is cited by both the Union brief at page 11 and the Franco brief at p. 36, with the Union brief quoting a portion of the opinion deemed favorable to the appellees' position. Judge Ray had more to say at pp. 762,3:

> "If litigation is necessary, and one /trustee/ refuses to be a complainant, he may be made a party defendant and the action proceed. In such case there is no nonjoinder of parties complainant, and in such case one of the trustees holding jointly may maintain the action. This shows that all are not necessary and indispensible parties complainant under all circumstances and conditions. That case is an exception to the general rule that all the trustees must be complainants.
>
> "In 1 Foster's Federal Practice, 182, § 59, we find the following:
>
> "'Relaxation of rule as to parties in special cases - The rules upon the subject of parties are, however, very loose, and the questions arising under them are de-

"'cided largely in the discretion of the court. The necessity for the relaxation of the rule is more especially apparent in the courts of the United States, where, oftentimes, the enforcement of the rule would oust them of their jurisdiction and deprive parties entitled to the interposition of a court of equity of any remedy whatsoever. * * * "

The Court was careful to consult the principle now constituting the fourth criterion of Rule 19(b), id. at 763:

> "Again, there is no necessity for a departure from the ordinary rules and practice. The property and all the parties are within the jurisdiction of the courts of the state of New York, and its courts are open and have jurisdiction of the subject matter. * * * "

As we pointed out in our main brief, in addition to the criteria of Rule 19, FRCP, all of the considerations we have urged for validating federal question jurisdiction argue for retention of the case on diversity grounds should the Court decide that federal question jurisdiction has not been established here. This was a consideration that the Court below conceded "might have some force" (92a) but for its erroneous conception that it had no discretion in the matter.

No floodgates of diversity cases would be opened by the careful and considered application of Rule 19, FRCP, plus the high degree of federal law issues implicit in the determination of the case assuming, arguendo, a determination of no federal question jurisdiction. We revert again to the language of Judge Ray in Caylor v. Cooper, 165 Fed. 757,762:

> "I do not understand it to be the policy of the law or of Congress to discourage or prevent litigation in the federal courts when a proper case is presented. Congress has created and defined the jurisdiction of the Circuit Courts, and wisely placed limitations thereon, but this was not for the purpose of discouraging litigation in the federal courts."

POINT III

APPELLEES' POINT THAT THE ACTIONS OF THE NON-RESIDENT INDIVIDUALS CONSTITUTING FRAUD, SO LONG AS DONE IN THEIR "REPRESENTATIONAL" CAPACITIES AS TRUSTEES SOMEHOW RELIEVES THEM OF PERSONAL LIABILITY AND ALSO PUTS THEM OUT OF REACH OF "LONG ARM" STATUTES, IS NOT WELL TAKEN.

It seems to us hornbook law, not requiring any citation of authority, that acts of fraud and deceit done by individuals acting in a representational capacity, whether directly, or passively in the role of co-conspirators, are, ipso facto, the acts of the individuals making them personally liable, regardless of the effect on the entity or quasi-entity which they represent. While personal surcharge of trustees as such may be the way a trust gets reimbursed for liabilities fastened upon it by the wrongful acts of its representatives, the party injured by the tortious acts is entitled to proceed against a tortfeasor in his personal as well as representative capacity, and, depending on the adjudication,, to recover a personal as well as representational judgment against him, or any permutation of the two.

In the light of the overwhelming authority holding it unnecessary to join all joint tortfeasors, we feel it is our right, should both of our first two points herein not be sustained by this Court, to continue so much of our first cause of action as pleads a case for fraud and deceit against the non-resident defendants in their individual capacities. We think, contrary to the arguments of appellees, that the district court would have diversity jurisdiction in a suit, as of right, against the non-resident defendants as individuals who would

also be personally answerable to the service of process under § 302(a)(2) and (3) of the New York Civil Practice Law and Rules. In that connection it seems obvious to us that Lehigh Valley Industries v. Birenbaum, 527 F. 2d 87 (2d Cir. 1975) dealing as it does with a non-resident business man having only casual contacts with the State of New York, sued in a commercial matter, can have no adverse impact on the obvious personal long-arm jurisdiction over non-resident trustees regularly administering a New York based trust in a suit for their tortious acts committed in their administration of their trust.

The portion of this suit which lies against the non-resident defendants (which, of course, does not include the second cause of action) is maintainable as of right, and yet its existence as the last resort alternative open to PPS only underlines the desirability of maintaining the unity of the case under the earlier points of this brief.

In any event we feel that the opinion below cannot stand uncommented upon and as a confirmed authority for the propositions that:

1. All trustees of a trust are, for purposes of determining diversity jurisdiction, indispensible parties (94a,95a).

2. A trustee signing contractual documents for a trust is a necessary party to litigation involving the contract even though his presence would defeat diversity jurisdiction (97a,98a).

3. The tort of fraud and deceit practiced by trustees in their representative capacities does not give rise to personal jurisdiction of them as individuals (98a).

4. A complaint alleging the details of fraud and deceit practiced by trustees as individuals acting in concert and conspiracy with one another, is nevertheless, in advance of discovery

and trial, dismissible for failure to plead fraud "with particularity" with respect to the specific acts imputed to each defendant (98a).

CONCLUSION

WE RESPECTFULLY URGE THE REVERSAL OF THE ORDER AND JUDGMENT OF DISMISSAL HEREIN, AND FURTHER URGE THE REMAND OF THE CAUSE FOR FURTHER PROCEEDINGS IN REGULAR COURSE.

Dated: New York, New York
November 16, 1976.

Respectfully submitted,

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HOROWITZ

STATE OF NEW YORK)
: SS.
COUNTY OF RICHMOND)

ROBERT BAILEY, being duly sworn, deposes and says, that deponent is not a party to the action, is over 18 years of age and resides at 286 Richmond Avenue, Staten Island, N. Y. 10302. That on the 17 day of Nov. 1976 deponent served the within Reply Brief upon

Proskauer, Rose, Goetz & Mendelsohn, Esqs.
and
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the address(es) designated by said attorney(s) for that purpose by depositing 3 copies of same enclosed in a postpaid properly addressed wrapper, in an official depository under the exclusive care and custody of the United States post office department within the State of New York.

ROBERT BAILEY

Sworn to before me, this 17 day
of Nov. , 1976

WILLIAM BAILEY
Notary Public, State of New York
No. 43-0132945
Qualified in Richmond County
Commission Expires March 30, 1978